# Recommendation of the Council for the Good Design of Defined Contribution Pension Plans

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## Background Information

The Recommendation for the Good Design of Defined Contribution Pension Plans was adopted by the OECD Council on 23 February 2022 on the proposal of the Insurance and Private Pensions Committee (IPPC). The Recommendation aims to assist Adherents in designing both occupational and personal pension plans in which retirement income depends on contributions paid, investment returns, and the way assets are paid out over retirement (defined contribution pension plans). It also aims at improving the robustness of retirement systems and building trust by ensuring people's best interest is taken into account.

***The OECD Roadmap for the Good Design of Defined Contribution Pension Plan***

The Working Party on Private Pensions (WPPP), a subsidiary body of the IPPC, developed and approved in 2012 the OECD Roadmap for the good design of defined contribution pension plans. These type of retirement plans are increasingly an integral part of most countries' overall pension system, and in some countries, they are the main component of their pension system. Therefore, overall retirement income adequacy depends on the retirement income stemming from these plans. The Roadmap was thus developed to provide guidance on ensuring that they were designed carefully.

Many governments, industry and pension providers have used the Roadmap over the years to guide policy, and, as a result, it has become an important standard in the world of retirement and pensions. The secretariat has also used the Roadmap to provide support to countries in order to improve the design of DC pension plans in several instances, via technical assistance projects and pension reviews.

The WPPP decided to revise the Roadmap to incorporate all the work conducted over the years since and to maintain its relevance given current contextual realities and the cumulated experience observed in OECD jurisdictions. The ten principles on improving the design of defined contribution pension plans have been either amended or revised to reflect additional work that the Secretariat and the WPPP have carried out since the initial guidelines were agreed upon back in 2012.

The Secretariat submitted to the WPPP at the June 2019 meeting a proposal to discuss how to update and improve the Roadmap. The WPPP was consulted on several drafts at its meetings and through a written consultation. A public consultation took place between 3 March and 14 April 2021. Respondents included actuaries, accounting and consultancies, asset managers, insurance companies, pension fund industry representatives, academics, and union representatives. The fourth and final version of the draft revised Roadmap was approved by the WPPP on 15 June 2021.

***The elevation of the Roadmap as an OECD Recommendation***

Given the relevance and wide use of the Roadmap, and the fact that it had become a main instrument for pension design policy, the WPPP and its parent Committee, the IPPC, decided to embody the Roadmap into an OECD Recommendation to be adopted by the Council on a proposal by the IPPC. The rationale was in particular to align the status of the Roadmap with the Recommendation on Core Principles of Private Pension Regulation [OECD/LEGAL/0429] as the Roadmap aims to improve the robustness of retirement systems and build trust by ensuring pension plans consider people's best interest. Another rationale for the proposal is to elevate the status and visibility of the Roadmap as a Recommendation, enhance its global reach, and provide for a regular report to the Council on the implementation, dissemination and continued relevance of the Recommendation.

Building on the revised Roadmap, a draft Recommendation was approved by the WPPP at its 6 December 2021 meeting and by the IPPC by written procedure on 7 January 2022 for transmission to the Council for adoption.

***Scope of the Recommendation***

The Recommendation provides ten high-level policy principles to strengthen retirement income adequacy were retirees depend on a Defined Contribution pension plan. Furthermore, the Recommendation aims to improve the robustness of retirement systems and increase beneficiaries' trust that pension provides have their best interest in mind.

The Recommendation also explicitly recognises the differences of the Adherents' national pension systems, and therefore allows for flexibility in its implementation based on the legal, policy, and institutional frameworks.

***Next steps***

The Recommendation will be launched at the next meeting of the WPPP scheduled for June 2022 and it will be use to provide technical assistance and policy guidance to Adherents.

The IPPC, through the WPPP, will report on the implementation, dissemination and continued relevance of the Recommendation to Council in 2027.

*For further information please consult: "Improving the design of retirement saving pension plans" (https://www.oecd.org/daf/fin/private-pensions/designingfundedpensionplans.htm).*

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**THE COUNCIL**,

**HAVING REGARD** to Article 5 b) of the Convention on the Organisation for Economic Co-operation and Development of 14 December 1960;

**HAVING REGARD** to the standards developed by the OECD in the area of pension regulation, financial consumer protection and financial literacy;

**CONSIDERING** that occupational and personal pension arrangements in which retirement income depends on contributions paid, investment returns and the way assets are paid out over retirement, such as defined contribution plans are increasingly an integral part of most countries' overall pension system, and in some countries they are the main component of their pension system;

**RECOGNISING** that overall retirement income adequacy depends, among other things, on the retirement income stemming from these pension plans;

**RECOGNISING** that Members and non-Members having adhered to this Recommendation (hereafter the "Adherents") have different legal, policy, and institutional frameworks that affect the extent to which they can implement this Recommendation;

**CONSIDERING** that the that the present Recommendation builds upon the experience in implementing the OECD Roadmap for the Good Design of Defined Contribution Pension Plans, approved by the Working Party on Private Pensions in 2012 [DAF/AS/PEN/WD(2012)10] and revised in 2021 [DAF/AS/PEN/WD(2019)17/REV3], and which is embodied in the present Recommendation.

**On the proposal of the Insurance and Private Pensions Committee:**

**I.** **RECOMMENDS** that Adherents design both occupational and personal pension plans in which retirement income depends on contributions paid, investment returns and the way assets are paid out over retirement, such as defined contribution plans (DC), with a view to improve the robustness of retirement systems and build trust that peoples' best interest is taken into account. To that effect, Adherents should:

1. **Design DC pension plans that are coherent with their long-term purpose and role in the pension system**. The design should promote resilience against shocks and be stable to provide certainty and instil confidence over the long term. It should also be consistent with the other components of the pension system and its objectives, and be coherent across the accumulation and pay-out phases. Policy makers should regularly assess current and potential retirement incomes taking into account broader economic and demographic factors and risks to assess whether DC plans are able to fulfil their role in meeting adequacy objectives.

2. **Make DC systems as inclusive as possible**. Where mandatory enrolment is not considered opportune, automatic enrolment, covering all employees and possibly the self-employed, can enhance participation while giving individuals the possibility to opt out. Financial incentives are also useful tools to promote savings for retirement. Using default options and offering a limited number of options for the contribution rate, the investment strategy and the pay-out can simplify decisions when members need to make them and encourage participation. Policy makers should avoid eligibility criteria that may disadvantage specific groups such as women and people in non-standard forms of work. They should also take care when considering design features that may make saving for retirement attractive (e.g. guarantees and early access to funds), but may end up reducing retirement income. Any early access to retirement savings should be a measure of last resort and based on individuals' specific hardship circumstances.

3. **Ensure total contributions are sufficiently high to achieve retirement income objectives**. Automatic and gradual increases to contribution rates can help members to reach appropriate contribution levels over their career. Flexibility regarding the level and timing of voluntary contributions could allow individuals to save based on their capacity, leading to higher overall contributions. Employer matching contributions can also promote employee contributions, while technology can help members to contribute

more by simplifying the contribution process and providing access to affordable financial planning. Encouraging members to contribute for longer by starting early and postponing retirement improves their chances of reaching their desired retirement income, particularly when life expectancy increases.

4. **Design financial incentives to maximise the impact on enrolment and contributions**. Tax rules should at least not discourage individuals to save for retirement. They should be straightforward, stable and common across retirement saving plans to avoid confusion. The design of financial incentives should reflect the retirement saving needs and capabilities of different population subgroups. Middle-to-high income earners tend to respond to favourable tax treatment, while low-income earners may be more likely to respond to matching contributions and fixed nominal subsidies. The incentives should be updated regularly to maintain the attractiveness of saving for retirement.

5. **Promote low-cost and cost-efficient retirement arrangements in both the accumulation and pay-out phases**. It is essential to promote initiatives to foster competition and to improve disclosure, comparability, and transparency. They may need to be complemented with appropriately designed pricing regulations and structural solutions that protect members' interests. Structural solutions should have strong institutional and governance frameworks, and can include tender mechanisms, allocation of individuals to quality low-cost providers, cost-efficient consolidations, large industry-wide non-profit providers, and independent centralised provider. Measures to promote cost-efficiency should balance the benefits of fair competition and economies of scale with the risks of an oligopolistic outcome. Finally, fees charged to participants should be aligned with the costs providers incur and the value provided to participants.

6. **Ensure that all individuals have access to appropriate and sustainable investment strategies and a well-designed default, where applicable**. For people unwilling or unable to choose, a default investment strategy should be established in line with the objectives of the DC pension system and the structure of the pay-out phase. For example, life cycle investment strategies can be well suited to encourage members to take on some investment risk when young, and to mitigate the impact of extreme negative outcomes when close to retirement. For people willing to choose their investment strategy, different investment horizons and risk profiles should be offered. To assess and monitor the appropriateness of different investment strategies against a policy objective, labour, financial, economic, demographic, environmental, social and governance (ESG) and other long-term sustainability risks affecting DC pensions should be considered.

7. **Ensure protection against longevity risk in retirement**. DC pension plans should provide some level of lifetime income as a default for the pay-out phase, unless other pension arrangements already provide for sufficient lifetime pension payments. Lifetime income can be provided by annuities with guaranteed payments or by non-guaranteed arrangements where longevity risk is pooled among participants. The choice of the type of arrangement will depend on the desired balance between the cost of guarantees and the stability of retirement income. Flexibility could be provided by allowing for partial, deferred or delayed lifetime income combined with programmed withdrawals. Full lump-sums should be discouraged in general, except for low account balances or extreme circumstances.

8. **Facilitate the regular monitoring and management of longevity risk**. Providers of lifetime pension income should use appropriate and regularly updated mortality assumptions that account for future improvements in life expectancy. Public authorities should make regularly updated population mortality data available to provide a reference for setting mortality assumptions. This data should be as granular as possible to facilitate setting appropriate assumptions and the development of sustainable retirement solutions for specific populations, for example to provide better value to low socioeconomic groups or those in poor health. Standardised, publicly and readily available data can promote effective risk management and facilitate the creation of standardised longevity indices that can be used to price the transfer of longevity risk to a third party.

9. **Ensure effective, personalised, regular, consistent and unbiased communication to members**. Communication with members should be clear and simple, with minimum jargon, especially when explaining potential options. It should also be timely and aligned with a purpose. Personalised information through online platforms or pension statements should ideally combine all pension sources and include

projections to update members and nudge them to take action to boost their pension adequacy. Projections should focus on potential retirement income levels in real terms, account for the likelihoods of different outcomes, and convey risks to plan members. Assumptions and methodology should be fully disclosed. Comparison tools should provide standardised information to allow users to compare performance, costs, investment allocation, and potentially other plan features, such as ESG factors. Policy makers should ensure that information provided by financial advisors and digital advisory services is accessible, accurate and unbiased.

10. **Promote awareness and support financial education about retirement and pensions**. Adherents should have national financial education strategies, which include a focus on raising awareness and knowledge about the importance of saving enough for retirement, the different options available, and risks like longevity. Financial education is a continuous process, which should include focused messages that evolve along with savings objectives at different life stages. Public authorities should seek to improve people's understanding of how the pension system works and explain pension reforms, as well as their economic rationale, through various means like communication campaigns. National communication campaigns should be driven by and evaluated against clear, realistic and well-targeted objectives.

**II.** **ENCOURAGES** stakeholders other than governments, for example the pension industry, to follow and promote the use of this Recommendation.

**III.** **INVITES** the Secretary-General to disseminate this Recommendation.

**IV.** **INVITES** Adherents to disseminate this Recommendation at all levels of government.

**V.** **INVITES** non-Adherents to take account of and adhere to this Recommendation.

**VI.** **INSTRUCTS** the Committee, through its Working Party on Private Pensions, to:

a. Serve as a forum for exchanging information on progress and experience with respect to the implementation of this Recommendation, fostering dialogue with and among stakeholders, and building on its work improving the design of defined contributions pension plans, as well as extracting lessons and best practices from it;

b. Conduct further work on the implementation of this Recommendation, in particular through the development of an implementation toolkit as well as voluntary reviews using this Recommendation as a benchmark;

c. Report to the Council on the implementation, dissemination and continued relevance of this Recommendation and report to Council no later than five years following its adoption and at least every ten years thereafter.

## About the OECD

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- **Substantive Outcome Documents** are adopted by the individual listed Adherents rather than by an OECD body, as the outcome of a ministerial, high-level or other meeting within the framework of the Organisation. They usually set general principles or long-term goals and have a solemn character.
- **International Agreements** are negotiated and concluded within the framework of the Organisation. They are legally binding on the Parties.
- **Arrangement, Understanding and Others**: several other types of substantive legal instruments have been developed within the OECD framework over time, such as the Arrangement on Officially Supported Export Credits, the International Understanding on Maritime Transport Principles and the Development Assistance Committee (DAC) Recommendations.